UNITED STATES DEPARTMENT OF AGRICULTURE
FARM CREDIT ADMINISTRATION
WASHINGTON, D. C.

SUMMARY OF CASES

RELATING TO

FARMERS' COOPERATIVE ASSOCIATIONS

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TABLE OF CONTENTS

DISCOUNTS DEDUCTIBLE - INCOME TAXES

In the case of Polley v. Westover, 77 F. Supp. 973, the plaintiffs paid income taxes under protest and then filed a suit against the Collector of Internal Revenue for their recovery.

The plaintiffs were engaged in the wholesale liquor business. In accordance with the custom of the trade and pursuant to agreements providing therefor, they gave quantity discounts to purchasers of liquor. The income taxes paid by the plaintiffs were demanded on the theory that the plaintiffs were not entitled to deduct or exclude the amount of the quantity discounts which they had given to purchasers of liquor in computing their income taxes. The following quotations are taken from the opinion in this case:

"In negotiating with the retail dealers for the sale of liquor, Frank Polley would agree that, upon receipt of a check for the invoiced price of the liquor, he would simultaneously transmit to the retail dealer in cash a certain percentage of the invoiced price, depending upon the quantity of liquor purchased.

"Polley Bros. Distributing Co. transmitted cash equal to five per cent of the invoiced price to retail dealers who purchased less than $500 worth of liquor, seven and one-half per cent to purchasers of between $500 and $750 worth of liquor, and large accounts purchasing more than $1,000 worth received ten per cent of the invoiced price in cash.

"Retail dealers were all treated equally, based upon the quantity of liquor purchased, without regard to whether or not they purchased their liquor exclusively from Polley Bros. Distributing Co. No discrimination or preference was made with respect to the products of any particular distiller.

"These payments to retail dealers of a percentage of the invoiced price in cash for quantity purchases were in accord with an established trade custom of wholesale liquor dealers in the Fourth Board of Equalization District, to wit: Santa Barbara, Ventura, Los Angeles, San Bernardino, Riverside, Orange, San Diego, and Imperial Counties, where Polley Bros. Distributing Co. made its sales. Competition among wholesale liquor dealers was such that a dealer could not secure an order for liquor unless he agreed in advance to reduce the price of the liquor by paying in cash an agreed percentage of the invoiced price for quantity purchases. It was necessary for Polley Bros. Distributing Co. to give such quantity discounts in order to sell liquor to its retail customers, R. 24, 61. (Underscoring added.)

"After Polley Bros. Distributing Co. received an order, the liquor would be delivered during the week, and the following week, when Frank Polley called to take the next order, he would receive a

check for the invoiced price of the merchandise delivered during the past week. In accordance with the previous agreement with the dealer, he would simultaneously transmit to the retail dealer in cash the percentage agreed upon with respect to the quantity of liquor purchased. A record of all such payments was kept in a memorandum book of Polley Bros. Distributing Co., and such payments were carried in the general ledger under the heading of 'sales expense'."

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"The trade custom which was followed by the Polley Bros. Distributing Co., of reducing the invoiced price of liquor by cash payments for quantity purchases, was known to, and followed generally by, wholesale and retail liquor dealers in the Fourth Board of Equalization District during the year 1941. The existence of this trade custom was known to the officers, employees, and members of the State Board of Equalization, to the competitors of Polley Bros. Distributing Co., and to the wholesale and retail trade generally. Such payments were a matter of common knowledge in the trade and to the State Board and were not secret."

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"The sum of $17,632.26, which was paid by Polley Bros. Distributing Co. in cash to retail dealers as quantity discounts during the year 1941 in reduction of the sale price of liquor, was an ordinary and necessary business expense within the meaning of Section 23 (a) of the Internal Revenue Code."

* * * * * *

"The allowance of an income tax deduction for such payments would not frustrate any well-defined national or state policy, Commissioner of Internal Revenue v. Heininger, 320 U.S. 467, 64 S. Ct. 249, 88 L. Ed. 171.

"Failure to allow this deduction would result in taxing the plaintiffs on amounts which they did not receive, and which, by agreement, they were not entitled to receive, because they agreed in advance with the retail dealers to reduce the purchase price of liquor by the amount of the cash payments." (Underscoring added.)

Attention is called to the fact that income taxes were demanded and paid under protest on the total amount of the discounts involved, namely, $17,632.26. The Court, however, held that this was error, and that this amount was deductible as an ordinary and necessary business expense under section 23 (a) of the Internal Revenue Code.

In view of the fact that it was established that the plaintiffs were obligated to give the discounts in question, it would appear that the

amount of the discounts was excludable on the theory that the discounts did not constitute income to the plaintiffs. Not all expenses incident to the operation of a business are deductible in computing income taxes because, under the terms of section 23 (a) of the Internal Revenue Code, only ordinary and necessary expenses may be deducted (See "Ordinary and Necessary Expenses," Summary No. 32, page 1), but all amounts that do not constitute income are excludable.

No reason is apparent why the amount of the discounts in question was not excludable on the theory that it did not constitute income, and hence no income taxes could be required to be paid thereon. The discounts had to be allowed in order to ascertain the exact sale prices of the liquor. Hence, the amount at no time apparently had the status of income. It is true that exclusions are sometimes loosely referred to as deductions, which, of course, in a sense is correct. But the right to make a technical deduction depends squarely on whether the statute provides for the making of such a deduction, while an exclusion is entirely independent of statute and depends only on whether the amount involved represents income. If it is not income, it is excludable. (See Wilcox v. Commissioner of Internal Revenue, 327 U.S. 404; also Associated Grocers of Alabama v. Willingham, 77 F. Supp. 990, Summary No. 40, page 1.)

PROFIT-SHARING AGREEMENTS - INCOME TAXES

In the case of Hammond v. Maloney, 80 F. Supp. 212, one of the questions for decision was whether amounts, based on profit-sharing agreements which the plaintiff, a contractor, had agreed to pay to two employees were deductible as ordinary and necessary expenses in computing his income taxes. The amounts in question were a percentage of the profits of the contractor's business and were to be ascertained as of the close of the contractor's fiscal year.

In one of the profit-sharing contracts, provision was made that the employee would not be permitted to "withdraw in excess of Ten Thousand Dollars ($10,000.00) per year" and that "Any funds amounting to more than $10,000.00 per year shall be permitted to remain in the company, to be used for working capital for use in the contracting and constructing business of the First Party." (Underscoring added.) The contract further provided that if the employee should sever his connections with the contractor and should "desire to withdraw the earnings accumulated to his account, he will give one year's written notice thereof to the First Party, and the First Party will not be obligated to pay such funds to the Second Party until one year after receipt of said written notice from the Second Party." (Underscoring added.) The share of the profits earned by the two employees of the plaintiff during the 1942 tax-year amounted to $86,635.88 and to $77,366.37 for the 1943 tax-year. The plaintiff paid the amount of taxes required by the Collector of Internal Revenue and filed a suit for the recovery of the amounts which the plaintiff alleged were illegally collected, including income taxes paid on amounts that the plaintiff was obligated to pay the two employees under the profit-sharing agreements with them.

In holding that the Collector of Internal Revenue erred in collecting income taxes on the share of the profits the plaintiff was obligated to pay the employees under the profit-sharing agreements, the Court said in part:

> "The defendant is not entitled to set off against plaintiff's claim for refund any claim for additional tax arising out of the accrual of the Mason and Peterson share of the profits in the tax years in question because (a) the said set-off was not interposed timely and no showing of diligence for the failure to do so was made to the court, (b) the right of the Commissioner of Internal Revenue to assess additional tax by reason of said transactions was barred by the statute of limitations at the time defendant attempted to interpose the set-off (the Commissioner of Internal Revenue did not at any time make any determination or assessment of any deficiency in income tax by reason of said transactions), and (c) upon the merits the Commissioner of Internal Revenue could not have lawfully assessed any deficiency in income tax by reason thereof." (Underscoring added.)

The arrangement in question, under which the taxpayer was obligated to make payments to the two employees based on the amount of the profits of the contractor, is analogous in some respects to the payment of patronage refunds by cooperative associations. Obviously, the amount of the patronage refunds to be paid with reference to any fiscal year may not be ascertained until the close of that fiscal year, and the same was true with reference to the share of the profits to be paid to the employees. In the case of the employees who were entitled to receive a share of the profits, this was of course paid to them as a part of their compensation and reduced the net profits accordingly.

In the case of patronage refunds, which must of course be paid in pursuance of a firm obligation to make them if they are to be excludable in computing the income taxes of a nonexempt corporation, they are excludable because they do not represent income. The obligation to make such refunds, which must exist at the time the transactions occur, as a result of which such refunds are made, keeps them from having the status of income, and hence, independent of statute, they are excludable in computing income taxes.

It seems to be well established that officers and employees of corporations may be paid in whole or in part on the basis of the earnings or profits of the corporations, and assuming that the amount of compensation thus received by them is reasonable in amount, such sums are deductible as ordinary and necessary expenses in computing the income taxes of the corporations involved. Under the Internal Revenue Code (26 U.S.C. 23 (a)), if the Bureau of Internal Revenue is of the opinion that the compensation of officers or employees is unreasonable in amount, it may refuse to permit a corporation to deduct, in computing its income taxes, more than a reasonable amount of compensation paid to an officer or employee. The leading case on this subject appears to be that of Botany Mills v. United States, 278 U.S. 282.

Attention is called to the fact that in the principal case under discussion, all amounts over $10,000 remained in the business and could not be withdrawn by the employee until one year after the receipt of a notice.

SOME RESULTS OF EXEMPTION

An agricultural cooperative association of producers, meeting the conditions of paragraph 12, section 101, 26 U.S.C., and confining its activities to those covered by that paragraph, is exempt from the payment of income taxes. It may pay dividends on its stock, if it is organized with capital stock, of not to exceed 8 percent per annum or the legal rate of interest in the State of incorporation, whichever is greater, and is not required to pay income taxes on account of such dividends. It may accumulate reasonable reserves for a necessary purpose without liability for income taxes on such reserves, but it should be obligated to account for and to allocate them to its patrons, members and nonmembers alike, on a patronage basis.

If an association is eligible for exemption, it is not required to pay income taxes on account of capital gains, such as might arise, for instance, from the purchase of a building for $10,000 and its sale for $15,000; but when such an association ceases to operate and is in dissolution, exemption ceases 1/, and capital gains are subject to income taxes. Such an association is also exempt from the payment of the documentary stamp tax of 11 cents per hundred dollars or fraction thereof on account of securities which it may issue. 2/

An exempt association may issue securities without the approval or consent of the Securities and Exchange Commission. 3/ It is not required to pay employment taxes with reference to any employee if the compensation for the services performed by any employee in the calendar quarter does not exceed $45. 4/

WITHDRAWING MEMBERS GOT NOTHING

In the case of Liggett v. Koivunen, decided by the Supreme Court of Minnesota, 34 N.W. 2d 345, the question for decision was whether members of a labor union who had withdrawn therefrom and joined another labor union were entitled to a part of the assets of the first labor union.

Local No. 49, International Brotherhood of Pulp, Sulphite, and Paper Mill Workers Union of International Falls, Minnesota, affiliated with the American Federation of Labor, by a vote of its members established a sick relief and benefit fund. At the time of the institution of the suit, the amount of this fund was about $20,000. Local No. 49, from 1916 to June 19, 1946, was the collective bargaining representative for

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1/ Summary No. 40, page 4.
2/ 26 U.S.C. 1808.
3/ 15 U.S.C. 77c(5).
4/ 26 U.S.C. 1607 (10)(A).

the "pulp and sulphite workers" unit of the Minnesota & Ontario Paper Company of International Falls, Minnesota. The C.I.O. organized a union of workers for the Minnesota & Ontario Paper Company, which, in an election conducted by the National Labor Relations Board, was chosen by workers for the Minnesota & Ontario Paper Company as their bargaining representative. At a meeting of Local No. 49, which was held on June 24, 1946, five days after the C.I.O. union had been certified as the new bargaining representative, a motion was made to amend the bylaws governing "the Sick Relief Association and Burial Benefit Association," which the Court held was really a part of Local No. 49 and not an independent organization. The Court found that the purported amendment "if carried into effect, would convert the benefit association, which up to that point had been nothing more than a fund or a department of Local 49 for the exclusive benefit of Local 49 members, into an organization existing wholly independent of Local 49 and operated for the benefit of all employees without regard to which union they belonged." Members of Local No. 49 then brought a suit to enjoin the carrying out of this bylaw. In this connection, it is important to keep in mind that the bylaws of Local No. 49 stated:

> ". . . that the purpose for which the benefit fund was established was to provide certain sick relief and funeral benefits for members of Local 49 whose dues are either paid up or are not in arrears for more than 60 days. In other words, no benefits were to be provided for nonmembers of Local 49 or for members thereof not in good standing." (Underscoring added.)

The Court in holding that the withdrawing members were not entitled to any part of the fund that had been established for sick relief and funeral benefits said in part:

> "It is well settled that the constitution and bylaws of an unincorporated association, if they are not immoral, contrary to public policy or the law of the land, or unreasonable, constitute an enforceable contract between the members by which their rights, duties, powers, and liabilities are measured. An individual in becoming a member impliedly agrees to abide by, and becomes a party to, this contract."
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> * * * * * * *
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> "As revealed by the terms of the bylaws adopted for the regulation of the sick relief and burial benefit funds, the members made a contract with each other pursuant to which these funds were raised for and dedicated to the organic purpose of providing sick relief and burial benefits only for the members of Local 49 who were in good standing. Here, the majority sought to make the benefits available for individuals outside the membership of Local 49. No bylaw provision authorizes a change in organic purpose by a mere majority vote. The rights of the minority established by contract with respect to either general or local property cannot be ignored. No number of the members of an unincorporated association less than the whole can divert the funds to purposes other

than those specified in the organization's constitution and by-laws. The majority undoubtedly can direct the use of the funds of the association within the scope of its declared purposes, and when there are two or more purposes for which the funds may be used the majority may select between them, but the majority cannot, against the will of the minority, lawfully divert such funds for uses other than those permitted by the constitution and by-laws. (Underscoring added.)

"Aside from any change in organic purpose, the attempted transfer of the benefit funds from Local 49 must fail. It is the general rule that the majority of the members of a local union (an unincorporated association) cannot, contrary to the wishes of a minority, transfer the funds of the local to another organization as long as the minority members (in excess of seven in number in this instance) continue their allegiance to the parent union and continue to function under the original charter issued by the parent union.

"Defendants assume, however, that the interest of individual members in the property of a local union is of such a nature that if a majority of them withdraw in a body they are then as a matter of equity entitled to have the property impressed with a trust for the purpose of distributing to the majority group a proportionate share. We have already emphasized that we are not confronted with the problem that would arise if Local 49 had been dissolved. A dissolution of the relation existing between a member and the local must be distinguished from a dissolution of the local itself. 4 Am. Jur., Associations and Clubs, § 56. We are likewise not dealing with a situation impregnated with an element of fraud. The majority members withdrew of their own free will. Issues that might arise out of fraud or out of dissolution of the local are not before the court. What rights, however, have individuals who withdraw as members of an unincorporated union? In Harris ex rel. Carpenters Union No. 2573 v. Backman, 160 Or. 520, 526, 86 P. 2d 456, 458, the court said: '* * * Like all other unincorporated voluntary associations by becoming a member unless the articles or laws of the association provide otherwise a person acquires not a severable right to any of its property or funds but merely a right to the joint use and enjoyment thereof so long as he continues to be a member.' (Underscoring added.)

"The general rule is that: 'in the absence of provisions in the constitution or by-laws giving members an individual interest in the assets of a voluntary association, members who withdraw thereby lose their rights to associate property, title to which stays in the members remaining in the association, and the rule applies whether membership is terminated by the member's own act or omission or by the act of the society. This rule applies even where a number of members secede in a body, and although they constitute a majority, and organize a new association. In such case the remaining members, and only they, are entitled to the entire funds and property of the association, so long as they continue to keep

it alive and adhere to its purposes.' 7 C.J.S., Associations, § 27b.

"In withdrawing from Local 49, the majority members voluntarily abandoned not only their membership status, but also the interest in the association property which that status gave them. Whatever enrichment has thereby been conferred upon the minority has been conferred without the exercise of fraud or of any other factor justifying equitable intervention by the court. Individuals who join a union or other voluntary association are reasonably chargeable with notice of the contractual membership obligations and liabilities which the constitution and bylaws impose, and they can be expected to foresee that they may at some future time wish to change their membership affiliation. It is not the province of a court of equity to rewrite or abrogate contracts to protect parties from those consequences which are attendant upon their voluntary abandonment of the contract and which consequences were reasonably foreseeable when the contractual obligations were assumed. 19 Am. Jur., Equity, §§ 33 and 70." (Underscoring added.)

The fundamental principles laid down by the Court are as applicable in the case of an unincorporated agricultural cooperative as they are in the case of any other type of voluntary association. Indeed, these fundamental principles would be applicable in the case of a nonstock incorporated cooperative association. It should be kept in mind that these fundamental principles are the ones that are applied in the absence of controlling provisions to the contrary. In the absence of valid provisions providing otherwise, members who withdraw from an incorporated or unincorporated association are not entitled to a portion of the association's assets at common law. (See "Legal Phases of Cooperative Associations," page 73.)

NEGOTIATIONS ONLY - NO CONTRACT

In the case of A. E. Staley Manufacturing Co. v. Northern Cooperatives, Inc., 168 F. 2d 892, the plaintiff brought suit against Northern Cooperatives to recover damages for the breach of two alleged contracts which it claimed it had entered into with Northern Cooperatives. Northern Cooperatives defended by successfully establishing that its negotiations with the plaintiff had never resulted in contracts and that the negotiations showed that any agreements to be entered into between the parties were to be evidenced by formal specific written contracts. The Court in holding that no contracts had been entered into and hence that Northern Cooperatives was not liable in damages to the plaintiff said in part:

"It seems clear therefore that the parties in their negotiations contemplated that the contractual relations and obligations between them should ultimately be witnessed by a specific written contract to be signed by them. This contract was required not only to be in writing, but was required to contain many specific limitations and restrictions. The orders, the oral negotiations, and the correspondence relative to this sale were negotiations

which were intended ultimately to result in the contracts upon which plaintiff has brought this action. An invitation to enter into negotiations is not an offer which may be accepted and thereby create a contract. Preliminary negotiations between parties who have in mind the execution of a formal written contract can not themselves be construed as constituting the contract. Nickel v. Theresa Farmers Co-op. Ass'n., 247 Wis. 412, 20 N.W. 2d 117; Dobbins v. City Bond & Mortgage Co., 343 Mo. 1001, 124 S.W. 2d 1111; Morrow v. De Vitt, Tex. Civ. App., 160 S.W. 2d 977; Moulton v. Kershaw, 59 Wis. 316, 18 N.W. 172, 48 Am. Rep. 516. In the law of contracts the intent of the parties must be looked to and a contract is not made so long as both parties anticipate that something remains to be done to establish contractual relations. As said by the author of the article on Contracts, 12 American Jurisprudence, Sec. 23, p. 519, 'A contract is not made so long as in the contemplation of both parties thereto something remains to be done to establish contractual relations.' (Underscoring added.)

"The author of the article on Contracts in 17 C.J.S., § 31, states the rule as follows: 'In order that there may be an agreement, the parties must have a distinct intention common to both and without doubt or difference. Until all understand alike, there can be no assent, and, therefore, no contract. Both parties must assent to the same things in the same sense, and their minds must meet as to all the terms. If any portion of the proposed terms is not settled, or no mode is agreed on by which it may be settled, there is no agreement.'

"In the same article at section 49, page 394, it is said: 'Unless all the terms and conditions are agreed on, and nothing is left to future negotiations, a contract to enter into a contract in the future is of no effect, as in case of a contract to enter into a contract on terms to be settled at some future time.'"

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"Notwithstanding that, plaintiff sent to defendant for execution the two proposed contracts reciting the delivery dates as changed by plaintiff's respresentative. This, not being in compliance with defendant's offer to purchase, was a rejection of that offer and the submission of an offer to sell. This offer submitted by the plaintiff was immediately rejected. Certainly, at this stage of the proceedings no contract had been entered into. Baird v. Pratt et al., 8 Cir., 148 F. 825, 10 L.R.A., N.S., 1116; Canton Cotton Mills v. Southwest Overall Co., 8 Cir., 8 F. 2d 807; Lewis v. Johnson, 123 Minn. 409, 143 N.W. 1127, L.R.A. 1915D, 150; Minneapolis & St. Louis Railway Company v. Columbus Rolling Mill Co., 119 U.S. 149, 7 S. Ct. 168, 169, 30 L. Ed. 376. But the proposed formal contract sent to defendant by plaintiff, being a rejection of defendant's offer, put an end to the negotiations and plaintiff could not thereafter accept defendant's original offer which had thus been rejected." (Underscoring added.)

ULTRA VIRES - OPTION CONTRACT VOID

In Trico Electric Cooperative v. Ralston, 196 P. 2d 470, decided by the Supreme Court of Arizona, it appeared that the electric cooperative, which had been formed with a view to obtaining loans from the Rural Electrification Administration, entered into an option contract with the Eloy Light, Power & Utility Company, under which the electric cooperative had the option during a period of sixty days to purchase for the sum of $200,000 all the electric transmission and distribution lines and facilities, and all water distribution properties of the Eloy Company.

Certain consumers of water and electric energy furnished by the Eloy Light, Power & Utility Company brought an action against the electric cooperative, and the Eloy Company asked for declaratory relief adjudicating (a) the option agreement between defendants, and (b) the contemplated sale and transfer of the property thereunder, to be unlawful, illegal, and void, and for injunctive relief enjoining defendants from consummating the sale and transfer of the property.

In trial court, the plaintiffs moved for judgment on the pleadings, which motion was granted by the Court. The Court held that the option and the contemplated sale thereunder were unlawful, illegal, and void, and of no force and effect. No injunctive relief was granted.

The electric cooperative appealed from the judgment, but the Eloy Company did not appeal. The electric cooperative urged that the Corporation Commission of the State and not the courts had the power to pass upon the validity of the option agreement. The Court, however, held that the powers of the Corporation Commission did not include authority to pass upon the validity of contracts and that the powers of the Corporation Commission in matters of this kind were restricted to determining if a sale would be in the public interest. In this connection the Court said:

> "Clearly the construction of a contract is a judicial function and the courts, not the corporation commission, have the jurisdiction to determine the validity of said option agreement, although eventually the contract of sale, if valid, must have the sanction and approval of the latter before it becomes effective."

The electric cooperative further argued that the question of whether the option agreement was ultra vires was a question that could be raised only by the State of Arizona, and that it could not be raised by the plaintiffs. The Court held, however, that the plaintiffs, as users of water and electric energy furnished by the Eloy Company, were entitled to "have the question of the validity of the contract affecting such utility service determined by a declaration of their rights, status and legal relations thereunder." In holding that the option contract was void because the electric cooperative had no authority in its charter to engage in the furnishing of water to anyone, the Court said in part:

"The articles of incorporation of defendant disclose that it has no charter power to engage in the business of furnishing water to any one, not even to its own members. With such limitations and restrictions, can the defendant lawfully contract for the purchase of the properties described in said option? To solve this problem we must interpret its articles of incorporation in accordance with well-established principles of law. (Underscoring added.)

"A corporation has only such powers as are expressly or impliedly conferred by its charter. Unlike a natural person, it may not do all things not expressly or impliedly prohibited, but must draw from its charter the power to act in any given respect, and can do only that which is expressly or impliedly authorized therein. A corporate charter is the index to the objects for which it was created and to the powers with which it has been endowed. The enumeration of certain powers operates as a limitation on such objects only as are embodied therein, and is an implied prohibition of the exercise of other and distinct powers, except such incidental powers as are reasonably necessary to accomplish the purposes for which it was organized. 19 C.J.S., Corporations, §§ 935, 939, pages 369, 371; 13 Am. Jur., Corporations, secs. 739, 743, pp. 770, 776. The charter of a corporation organized under general legislation consists of the provisions of the state constitution, the particular statute under which it is organized, and all other general laws which are made applicable to the corporation formed thereunder and its articles of incorporation. 18 C.J.S., Corporations, § 43. With respect to matters to which statutes do not apply, the articles of incorporation of the corporation control and are its fundamental and organic law. 18 C.J.S., Corporations, § 43. '* * * but in respect to those mattters to which the statute does not apply the articles of incorporation govern. * * *' Orme v. Salt River Valley Water Users' Ass'n., 25 Ariz. 324, 217 P. 935, 941. See also Norwegian Old People's Home Soc. v. Willson, 176 Ill. 94, 52 N.E. 41."

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"There is no reference to authority to furnish and distribute water for any purpose. Clearly the ownership and operation of a water utility is not within the powers granted by defendant's charter, and it is not alleged that said business is incident to or necessarily connected with the lawful purposes for which it was organized. (Underscoring added.)

"The rule is that a transaction ultra vires in the true sense, because beyond the power of the corporation to enter into it, is void and may not be validated by ratification or otherwise. The Supreme Court of the United States, in Central Trans. Co. v. Pullman's Palace Car Co., 139 U.S. 24, 11 S. Ct. 478, 488, 35 L. Ed. 55, announced such rule as follows: '* * * A contract of a corporation, which is ultra vires in the proper sense, that is to say, outside the object of its creation as defined in the law of

its organization, and therefore beyond the powers conferred upon it by the legislature, is not voidable only, but wholly void, and of no legal effect. The objection to the contract is not merely that the corporation ought not to have made it, but that it could not make it. The contract cannot be ratified by either party, because it could not have been authorized by either.'" (Underscoring added.)

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"Since the defendant contracted to purchase a water utility which by its charter it has no power to own and operate, the option agreement is ultra vires and void, and we need not consider or discuss the other matters urged by plaintiffs against the validity of said option agreement."

Every corporation, cooperative or otherwise, should confine its activities to those coming within the scope of its articles of incorporation. The failure to do this may adversely affect the corporation. The State in which a corporation is incorporated may always proceed against a corporation for exceeding its charter powers; at least members or stockholders who have not consented to the ultra vires act may restrain the corporation and its officers from exceeding its authority. Directors and officers of a corporation may incur personal liability for losses arising from exceeding the charter powers of the corporation.

In some instances, particularly in the Federal Court, third persons may in certain circumstances take advantage of the fact that a corporation is acting ultra vires. In United States v. American Livestock Commission Company, 279 U.S. 435, it was held that because the cooperative livestock association had transacted business with nonmembers, in violation of its charter, the association could not successfully complain of a boycott by dealers in livestock insofar as the nonmember business was concerned.

AGENT OR PURCHASER

The question for decision in the case of Fjeldahl, et al., v. Homer Co-op. Ass'n., et al., 11 Alaska Reports 112, was whether the association had acted as agent in the receipt, marketing, and sale of fish received from plaintiffs or whether the association had agreed to purchase outright the fish of the plaintiffs at fixed prices. The three plaintiffs had each purchased a share of stock in the cooperative association. No written contracts were entered into by the three plaintiffs with the cooperative association, and the oral understanding between the association and the plaintiffs did not specify whether the association was acting as agent or otherwise in the receipt and marketing of the fish. As shown by the following quotation from the opinion, the association, with the knowledge of the plaintiffs, entered into a contract called a sales agreement:

"Under this contract the purchaser Terranova agreed to purchase from the defendant Association, not only farm produce but also

marine sea foods of various types including salmon, clams, crabs and halibut 'at the f. o. b. price on dock set opposite each variety, as follow:

"'(1)	Salmon	
	Silver	17¢ per lb. dressed, head attached
	King	20¢ per lb. dressed, head attached
	Red	17¢ per lb. dressed, head attached
"'(2)	Clams	10¢ per lb. gross weight unshelled
"'(3)	Crab (Dungeness)	40¢ ea., minimum weight 1-1/2 lb. cooked
"'(4)	Halibut	Current wholesale marked price per lb., dressed and headless.'

"Terranova, in this contract, agreed to make payments to the Association through its manager or other authorized officer for all sea foods, farm products and produce delivered under the contract, on or before the 10th, 20th and 1st days of each month, payment to be made every ten days. Nothing in this contract explicitly or indirectly indicates that the Association was acting as an agent in the sale of the produce described therein, except for the statement that the Association was engaged 'in the marketing of such commodities.' But it appears likely that even if it was understood by all parties, including the persons who were then or thereafter members of the Association and who supplied halibut for sale to Terranova, that the Association was, in fact, acting as such agent, the contract would have been the same. The contract in and of itself does not define the real relations between the Association and its members with respect to the produce to be sold, including marine sea foods, which the Association, as seller, therein contracted to sell and deliver to Terranova as the purchaser. If the individual members of the Association actually remained the owners of the property covered by the contract until its delivery to Terranova, and the Association acted only as agent of its members, no inkling of the existence of any such arrangement may be gained from the reading of the contract itself."

The party, namely Terranova, who purchased the fish from the association, did not pay the association for all the fish delivered by plaintiffs, and plaintiffs brought suit against the association for the recovery of the balance which they claimed was due them on account of fish which they had caught and delivered. The plaintiffs also claimed a lien on the wharf of the association in pursuance of an Alaska statute on account of the fish which they had delivered to the association. The plaintiffs apparently claimed that statements made by the manager of the association showed that the association was the outright purchaser of the fish. 'In this connection the Court said:

"The plaintiffs insist that it was the understanding and agreement between themselves and the Association that the Association actually purchased the fish and did not act as a mere agent for making

sale to Terranova. As proof of their justification in that belief, they have testified to conversation with Sol Brososky [manager] in which the latter chidingly assured them that their 'responsibility' ended when the fish were delivered by the plaintiffs to him as manager of the Association on the wharf at Homer, and as to payment for the fish Brososky said: 'Leave it to me; that's my business.'"

Inasmuch as the capacity in which the association acted was not stated, the Court considered all the facts and circumstances and held that the association was the outright buyer of the fish and obligated to see to it that the plaintiffs were paid the prices which the buyer from the association had agreed to pay therefor.

In view of all the facts and circumstances, it is submitted that the Court could properly have held that the association was simply acting as agent in the handling of the fish and that it had not obligated itself in any way to pay to the plaintiffs the sale price of the fish, except as such sale price was received from the purchaser of the association. In this connection, attention is called to the following quotation from the opinion:

"A circumstance tending to support the contention of the defendant, and militating to an equal degree against the plaintiffs, is that the Association, to the knowledge of all of the plaintiffs, was to charge and did charge only 10% for its services in connection with the sale or marketing of the halibut supplied by the plaintiffs. All concerned understood that to be the fact, and it was the fact. The receipts issued by the co-op to the plaintiffs specified the prices which the plaintiffs were to receive for the halibut, as 10% under the market price. And so it may be validly argued that this limitation of compensation for the Association was adequate warning to the plaintiffs that the Association did not purchase the halibut on its own account but only acted as agent of the plaintiffs and other fishermen in making sale of the product. The argument is far from being conclusive because it must also be considered that even though the Association was buying the fish on its own account, it might conceivably, even probably, agree to limit its profit to 10% in order to persuade the plaintiffs to sell their fish to the Association.

"Another circumstance operating against the plaintiffs and in favor of the Association lies in the fact that the plaintiffs made inquiry of Sol Brososky, possibly of others, whether or not any bond had been furnished or insurance given that the defendant Terranova would pay for the fish sold to him. This inquiry might indicate that the plaintiffs knew, or understood, or at least suspected, that they were not to be paid unless Terranova paid the Association and, therefore, that the Association was really acting as agent for the plaintiffs and other fishermen. Against this it may be urged with equal force that the plaintiffs, by their own observation, could see that the Association was without any considerable means or property, and that even if the Association were

buying for itself, unless Terranova paid the Association, the fishermen were likely to remain unpaid because the Association had no money and no means out of which to pay for the fish. Therefore, even though it was understood between the parties, or was understood by the fishermen, that they were selling to the Association and not to Terranova, and that the Association was acting for itself and not as agent, they still naturally might have made inquiry about a bond to guarantee the payment by Terranova for the fish he bought."

It is believed that the only reported case in the United States that is analogous to the case under discussion is that of Haarparinne v. Butter Hill Fruit Growers' Ass'n., 122 Me. 138, 119 A. 116. In that case the Court held that as the contract between the association and the member did not state the capacity in which the association acted, the association was not the purchaser of the apples involved but was functioning on an agency basis, and therefore was not liable to the plaintiff for the market price of apples which froze.

Under the normal purchase and sale marketing contract, the association is required to account to its members only on the basis of the amounts received by the association for the agricultural commodities in question. In other words, if an association acting in good faith and with reasonable care - to take an extreme case - has not received anything for the agricultural commodities received from its members, it would not normally be liable to its members for any amount. Associations that ordinarily use marketing contracts do not agree to pay their members the market price for commodities delivered by them, but are simply obligated to account on the basis of the price received by the association for the commodities involved.

"FREE EXCHANGE OF IDEAS" - LABOR DISPUTE

In National Labor Relations Board v. Enid Co-op. Creamery Ass'n., 169 F. 2d 986, that Board instituted proceedings for the enforcement of an order which it had issued against the cooperative association. This resulted from action to organize the employees of the cooperative. The cooperative posted a sign against soliciting union membership, talking union business on company time or on its premises. The supervisory employees of the cooperative also made statements to the employees for the apparent purpose of persuading them against joining the union.

On account of these facts the National Labor Relations Board issued an order against the cooperative directing it to cease and desist from interfering with, restraining, or coercing its employees in the free exercise of their collectible bargaining rights, and specifically directing that the "no solicitation" rule be rescinded.

The Board then petitioned the Circuit Court of Appeals to enforce its order, and that Court remanded the case on account of the fact that the Supreme Court of the United States in Republic Aviation Corp. v. N.L.R.B., 324 U.S. 793, 65 S. Ct. 982, 988, 89 L. Ed. 1372, 157 A.L.R.

1081, had expressed the view that a rule prohibiting to solicitation outside working hours, although on company property, "must be presumed to be an unreasonable impediment to self-organization . . . in the absence of evidence that special circumstances make the rule necessary in order to maintain production or discipline." (Underscoring added.) This action was taken so that testimony might be taken by the National Labor Relations Board to see if special circumstances justified the issuance of this "no solicitation" rule. The National Labor Relations Board, however, instead of taking testimony amended its order so as to delete therefrom the provisions relating to the rescission of the "no solicitation" rule. The Board then asked for the enforcement of its order as amended. In denying the relief sought for and in reversing the order of the National Labor Relations Board, the Court said:

> "In view of the failure of the Board to hear testimony on the issues framed by the order of remand, and the abandonment of its rescission order, we must presume that the order was, in the special circumstances, necessary to maintain production or discipline. Indeed, the record shows that the rule was permissibly invoked on at least one occasion for that purpose. The stated purpose of the notice was 'to maintain peace and harmony among our employees', and was intended to be in accordance with 'the policy of the union'. The notice went on to state 'we want our employees to know that it is not necessary to belong to any union to work for this Association, neither is it necessary to refuse to belong to a union to work for this Association. This is a question for each employee to decide for himself without pressure or prejudice from the union or the employer'. We can find nothing either overtly or covertly inimical in this statement. Cf. N.L.R.B. v. Virginia Electric & Power Co., 314 U.S. 469, 62 S. Ct. 344, 86 L. Ed. 348; Boeing Airplane Co. v. N.L.R.B., 10 Cir., 140 F. 2d 423; N.L.R.B. v. American Tube Bending Co., 2 Cir., 134 F. 2d 993, 146 A.L.R. 1017.
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> "The course of conduct of the respondents' supervisory employees relied upon by the Board to support enforcement consists of statements by them to employees during the union's campaign to organize the plant. The statements were made to various employees at their homes, on the street, and wherever they happened to meet. They were undoubtedly calculated to persuade the employees not to join the union. Thus, they were told that they would derive no benefit from joining a union; that the wages they were being paid were higher than the wages paid in similar plants, and that if the employees were unionized they might have to take a reduction in salary; that if they joined the union and failed to pay their dues they would be discharged, and other 'disadvantages' of union membership were pointed out. But, there is no evidence of any direct or subtle threats of coercion. No one was led to believe that membership in the union would affect his employment in any way, and there is no evidence whatsoever that membership in the union or membership activities prejudiced any employee.

"The Act proscribes interference, restraint and coercion - it does not proscribe 'free trade of ideas'. N.L.R.B. v. Virginia Electric & Power Co., supra; Thomas v. Collins, 323 U.S. 516, 65 S. Ct. 315, 89 L. Ed. 430. The Board has a wide latitude in appraising facts and drawing inferences therefrom. It has the primary responsibility for the administration of the Act and to that end, the right and duty to determine when facts constitute unfair labor practices. But we, along with the Board, have the duty to balance the employer's inalienable right of free speech and expression against the right of the employees to freedom of self-organization. See N.L.R.B. v. Continental Oil Co., 10 Cir., 159 F. 2d 326. In that process, we have said that so long as persuasion does not amount to coercion, it is within the guaranty, but that when words of persuasion are uttered by one who holds the power of coercion, it is often difficult to attain the delicate balance between the two. N.L.R.B. v. Continental Oil Co., supra. If, however, an employer has the right not only to inform but to persuade to action, see Thomas v. Collins, supra, he surely may tell an employee that, in his judgment, it would not be beneficial for him to join a union if he also makes it plain that such employee has a free choice without fear of reprisal.

"Judged by this test, we are convinced that the statements relied upon by the Board are wholly insufficient to warrant enforcement." (Underscoring added.)

Attention is called to the fact that the Labor Management Relations Act, 1947, sometimes referred to as the "Taft-Hartley Act," provides in 29 U.S.C. 158 (c) as follows:

"The expressing of any views, argument, or opinion, or the dissemination thereof, whether in written, printed, graphic, or visual form shall not constitute or be evidence of an unfair labor practice under any of the provisions of this subchapter, if such expression contains no threat of reprisal or promise of benefit."

The holding of the Court in the case under discussion insofar as exchanging ideas is concerned seems to approximate the rule stated in the statutory provision just quoted. The Labor Management Relations Act, 1947, does not appear to specifically deal with the "no solicitation" rule, and so the restrictions on this rule imposed by the Supreme Court in the Republic Aviation Corporation case referred to above would appear to be controlling.

Agricultural labor was excluded from the National Labor Relations Act and the exclusion was continued in the Labor Management Relations Act of 1947. In the opinion of the Court in the case of National Labor Relations Board v. John W. Campbell, Inc., 159 F. 2d 184, 187, it was said:

"Congress, as well as this Court, has recognized that the packing and preparing of agricultural products for the market is a necessary incident to any agricultural operation, for no farmer, dependent upon that which he produces to sustain his operations,

could long exist if he could not market that which he produces, and so long as the operation of washing, packing, and preparing for market by the employees of a farmer is on that only which he has produced on his farm, it is a necessary incident to farming and is agricultural labor. The wheat farmer must thresh his wheat; the cane grower must cut his cane and make its juice into syrup; the cotton grower must gin and bale his cotton; the citrus grower must pick and pack his oranges; and the tomato grower must do likewise. So long as these undertakings are in the preparation and packing by him for market of that which he has grown on his farm, the labor necessary thereto is agricultural labor." (Underscoring added.)